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Voluntary disclosure initiatives highlight need for offshore foreign bank and financial reporting

Through the past several years, the Treasury Department and Internal Revenue Service have made enforcement of foreign bank and financial account reporting obligations a top priority for both corporate and individual taxpayers. Reporting is required on the taxpayer's regular tax return and, if the account is over $10,000 at any time during the year, also reportable on a special form known as the Report of Foreign Bank and Financial Accounts (FBAR). The FBAR, filed electronically as FinCEN Form 114, is due **annually** by **June 30** for accounts maintained during the previous calendar year. Penalties for noncompliance can be extremely severe. In an effort to bring taxpayers with undisclosed foreign accounts into compliance with U.S. tax laws, the IRS has instituted several voluntary reporting procedures under which taxpayers can notify the IRS of offshore accounts and potentially face less severe penalties. In addition, under the Foreign Account Tax Compliance Act (FATCA), foreign financial institutions also are now reporting U.S. persons' foreign financial accounts to the U.S. government.

Background

On its federal income tax return, each United States corporation, partnership and individual must disclose the existence of any foreign bank or financial account if the taxpayer has a financial interest in, or signature or other authority over, the accounts. In addition, these taxpayers have a responsibility to file the FBAR (FinCEN From 114) by June 30 if the aggregate value of such accounts exceeded $10,000 at any time during the previous calendar year. Reporting is required even if the account is legitimate and all taxable income has been correctly reported. No extensions or retroactive relief are generally available.

The definitions of "financial interest" and "signature or other authority" are broad. Considering the extent of cross-border business relationships today, many companies, including even small to mid-size entities, are likely to maintain foreign bank accounts for which both the company and its officers must report. Reporting obligations could apply to an officer of a corporation, partnership or other business who maintains signature authority over the entity's foreign financial accounts. Officers of large publicly traded companies are sometimes exempt from filing and, in some situations, a corporate parent may fulfill reporting obligations for a U.S. subsidiary. There are few other exceptions available.

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Under FATCA, foreign financial institutions are required to disclose to the U.S. Treasury Department any U.S. account holders. Therefore, the U.S. government now has a backstop to voluntary taxpayer disclosure. Foreign banks have recently begun sending letters to account holders acknowledging that their existence may be reported to the U.S. Treasury.

Penalties

The Treasury Department may impose a civil penalty of up to $10,000 for each non-disclosure on any person who non-willful violates the reporting requirements. There is a narrow exception for a non-willful failure if the person's non-disclosure is due to reasonable cause. If the violation or failure to file is willful, there is no reasonable cause exception and the $10,000 penalty is increased to the greater of:

1. $100,000, or;
2. 50 percent of the balance in each unreported account at the time of the violation.

Willful failure to properly file the FBAR can also result in criminal penalties.

Voluntary disclosure of past violations

The IRS has instituted a series of voluntary reporting procedures under which a taxpayer can notify the IRS of offshore accounts. This program provides an opportunity to correct past FBAR and income tax reporting failures. Separate, more generous disclosure programs exist for U.S. nonresidents and individuals with very small accounts.

In light of the quickly approaching June 30 FBAR deadline and the window of opportunity provided by the IRS to make necessary corrections, taxpayers should take steps now to ensure compliance with these sometimes overlooked requirements.

For more information, please contact Mark Snider, David Tumen or any member of Porter Wright's International Tax Practice Group.